No. 77-255

In the
Supreme Court of the United States
OCTOBER TERM, 1977

SUNDSTRAND CORPORATION,
Petitioner,
vs.
SUN CHEMICAL CORPORATION, RAYMOND F. RYAN and THOMAS B. HART, JR., EXECUTORS OF THE ESTATE OF JOHN B. HUARISA,
Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Seventh Circuit

BRIEF OF RESPONDENTS IN OPPOSITION

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BRIEF OF RESPONDENTS IN OPPOSITION

QUESTIONS PRESENTED

Sundstrand presents questions for review (Pet. p. 3) which are illusory and, in reality, not presented in this case at all. As for question one, we are not dealing with a plaintiff who bought stock on the basis of concurrent causes but with a plaintiff who purchased stock solely because of a mistake of law. As for question two, we are not dealing with a plaintiff claimed to have acted negli-

gently, but with a plaintiff who has insisted it purchased stock because it was obligated to purchase it. As for question three, the Court of Appeals did not make an "independent study" of material not in the trial record so as to make findings contrary to the findings of the district court. The Court of Appeals, almost in disbelief, simply sought confirmation in the record on appeal that Sundstrand actually bought the Burke stock because it thought it was obliged to, and not for some other reason.

In reality, the only question presented by the Sundstrand Petition for Certiorari is whether the Court of Appeals decided this case correctly under all the circumstances, which of course is no basis for seeking yet another review.

STATEMENT OF THE CASE

Sundstrand's statement of the case is incomplete and in important respects unsupported by the record.

From the outset of this litigation Sundstrand sought to prove that on January 9, 1969, in the midst of merger negotiations with SKI, Sundstrand purchased 223,190 shares of SKI stock so as to prevent these shares from falling into unfriendly hands before Sundstrand had an opportunity to complete the merger negotiations. Sundstrand's case foundered, however, when all it could prove was that on January 9, 1969, it obtained an option to purchase the 223,190 shares which it need not have exercised (M.App. 17-18, 85-87); it did not buy the shares until February 6, 1969, two weeks after the merger negotiations were abandoned; on that day, without obligation, Sundstrand exercised the option, paid the $6,360,915 bal-

ance of the purchase price, and took title to the SKI shares.*

Other than to contend vigorously, but mistakenly, that it was legally committed to purchase the SKI shares on February 6, 1969, Sundstrand to this day has not explained what motivated it to buy the SKI stock when it was not obliged to buy it and when all reason for buying it had disappeared.

1. Sundstrand's Mistake of Law

Throughout the first eight years of this case, Sundstrand and its counsel have insisted unequivocally that Sundstrand was legally obligated by the January 9, 1969 agreement with Huarisa to complete the purchase of the Burke stock on February 6, 1969 (Sun App. 1-3, M. App. 17-18, 85-87). Innumerable instances where Sundstrand and its counsel have so asserted could be cited. For example, in closing argument before the district court Sundstrand's counsel, speaking for his client of course, stated flatly, "we were bound to pay" the $6,360,915 on February 6, 1969, "Our position is we were obligated to consummate the deal," "Well, your Honor, I can assure you that rightly or wrongly Sundstrand considered it had a legal obligation . . . and I don't back off from that." (S. App. 132, 133, 139).

Sadler, Sundstrand's president when he testified, conceded on cross-examination that shortly before February

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* Every court that has considered the question has ruled, over Sundstrand's strenuous opposition, that Sundstrand had no obligation to purchase the Burke stock. See M. App. 17-18, 85-87, and *Sundstrand Corp.* v. *Standard Kollsman Industries, Inc.*, 488 F.2d 807, 810 (7th Cir. 1973).

6, 1969, he had asked Ethington (his predecessor as president) what Sundstrand was going to do about the Burke stock and Ethington had responded that Sundstrand was going to purchase it because "our counsel feels we are obligated to buy the stock" (S. App. 120-122).*

Actually, the record in this case supports no explanation of Sundstrand's purchase of the Burke stock other than Sundstrand's mistake of law.** Sundstrand was so committed to the proposition that it was legally bound to complete the purchase of stock on February 6, 1969, that it offered no other explanation, or evidence, as to what induced it to pay $6,360,915 to the Burke family on that date. Save for Sadler's concession on cross-examination, not a single Sundstrand witness offered a word of testi-

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* Sundstrand answered an interrogatory, "Counsel for Sundstrand . . . who have participated in various aspects of the stock purchase transaction and represent Sundstrand in this action, *did not* render any opinion to Sundstrand that the agreement *did not* obligate it to make such payment at the time payment was made." (S. App. 122-127, 150). Emphasis supplied.

** During final argument the following colloquy occurred between the district court and counsel for Sundstrand (S. App. 143):

> "THE COURT: Let me ask this question—I think I know the answer without asking it, but is there any place in any deposition or transcript or trial testimony where any explanation was made by Sundstrand as to why they determined to go ahead with the Huarisa deal after they decided they were not going to go through with merger? Is there a single word of testimony in the record that would show the reason for proceeding?
>
> MR. MONTGOMERY: I don't recall any as such, your Honor, but there is testimony in the record that they thought that they had bought the stock on January 9th. . ."

mony on the subject (either in chief or in rebuttal). Ethington testified as to what induced Sundstrand to enter into the January 9, 1969 agreement, but he said nothing at all about why Sundstrand went ahead with the purchase of the Burke stock on February 6, 1969 (Sun App. 3-6).

On its own theory of the case, then, Sundstrand's purchase of the Burke stock was induced solely by its mistaken belief that it was legally bound to make the purchase.

2. Sundstrand's Adverse Information About SKI

Even before its survey and analysis of SKI which Sundstrand undertook during mid-January 1969, and which led to termination of merger negotiations, Sundstrand knew and was concerned about the fact that SKI was carrying a substantial amount of deferred costs on its books. The subject was discussed at virtually every meeting between the parties during November and December 1968 (Sun App. 6-13). The problem of SKI's deferred costs loomed so large that Sundstrand's president at the time, Ethington, personally directed the Sundstrand survey team to investigate and report on them (Sun App. 13-14). As early as January 10, 1969, the survey team, headed by then executive vice-president Sadler, regarded the problem as serious (Sun App. 14-18). By January 13, 1969, Sadler advised Ethington that he was very pessimistic about the merger (Sun App. 18-20). On January 20, 1969, the Sundstrand management concluded that SKI was carrying in excess of $4,000,000 of deferred costs on its books which it was not likely to be able to amortize against future business (Sun App. 21-38).

On January 20, 1969, Ethington and Schuette (then Sundstrand's vice-chairman) met with Huarisa and Meers to advise them that Sundstrand had decided to terminate the merger negotiations. It was explained that Sundstrand did not foresee that SKI's huge deferred costs could be amortized against future orders. Ethington summarized the reasons he gave Huarisa and Meers for terminating the negotiations (Sun App. 39-54):

> "We talked about products and new developments and the business in general, and that we did not think we were going to get the synergism we originally thought, and there were various reasons, but *basically,* that *we did not see how the earnings were going to be met because of the tremendous write-offs that were going to be faced by Standard Kollsman in our opinion.*" (Emphasis supplied)

On January 23, 1969, it was announced that merger negotiations between Sundstrand and SKI had been terminated by mutual agreement. (Sun App. 54-55) By this time, said the Court of Appeals (M. App. 82-83, 84-85, 104, 105), Sundstrand had sufficient adverse information about SKI to know that it was not justified in paying the $6,360,915 balance of the purchase price for the Burke stock if it was not obligated to do so.

3. Sundstrand Officials Make It Clear They Personally Do Not Wish To Own SKI Stock

Ethington and Sadler had secretly purchased substantial blocks of SKI stock during late December 1968, before merger negotiations between Sundstrand and SKI were known to the public. These Sundstrand officers became so disenchanted with the financial condition of SKI during the Sundstrand survey, however, that they

promptly determined to divest themselves of their holdings of SKI stock. Ethington sold his 2,000 shares on January 14, 1969. Sadler sold 1,000 shares on January 17, 1969, and 600 shares on February 13, 1969. Plainly, neither Ethington nor Sadler wished to be owners of SKI stock. (Sun App. 56-59)

4. The Discredited Theory That, Legal Obligation Aside, Sundstrand Purchased The Burke Stock On February 6, 1969 As An Investment

In desperation, Sundstrand urged (for the first time) in the Court of Appeals that, even if it were not obligated to buy the Burke stock, it completed the transaction on February 6, 1969 for "investment" purposes. As the Court of Appeals correctly observed (M. App. 103), this theory had been superimposed on Sundstrand's case by the district court, *sua sponte*.

The investment theory, however, is inconsistent with Sundstrand's insistence that it bought the Burke stock because it was legally obligated to purchase it. The theory is inconsistent with Sundstrand's announced intention that it would be interested in acquiring the Burke stock only if the merger was to be consummated. The investment theory is inconsistent with the fact that four days after Sundstrand bought the stock it began pressing Huarisa to take the stock off its hands (M. App. 103). And, apart from those inconsistencies, there is no evidence in this record that Sundstrand made a decision to invest $6,360,915 of its corporate funds in any SKI stock, let alone the Burke stock.

Moreover, as the Court of Appeals held (M. App. 103), the notion that, despite its negative findings about SKI,

Sundstrand decided to invest more than $6 million in SKI stock in February 1969, by purchasing 233,190 shares from the Burke family at $30 per share is too farfetched to warrant serious consideration. The market price for SKI stock on February 6, 1969 was about $25 per share, $5 per share below the price of the Burke stock. Thus, "investing" in the Burke stock meant investing in 223,190 shares of SKI stock at a premium over market of more than $1,000,000. In addition, the Burke stock was unregistered, as Sundstrand knew, and therefore a subsequent sale of this SKI stock would be likely to be at a substantial discount below market (as much as 50% according to Sundstrand's expert).

Finally, this theory that apart from the proposed merger, Sundstrand may have decided to invest $6,360,915 in SKI stock, is simply not the case presented by Sundstrand in the district court.

We wind up where we began: there is no explanation in the record for Sundstrand's purchase of the Burke stock on February 6, 1969, other than Sundstrand's unfounded belief that there was a legal obligation to purchase it.

5. The Decision of the District Court

The district court concluded, correctly, that in order for a plaintiff to prevail in a Rule 10b-5 case, he must prove not only that there were material misrepresentations or omissions, but that the misrepresentations or omissions caused his injury (M. App. 57).

The district court found causation in this case on the unsupported theory that Sundstrand purchased 223,190

shares of SKI stock in reliance upon material misrepresentations and omissions of SKI and Huarisa. Specifically, the court found that, in purchasing 223,190 shares and paying the Burke family $6,360,915 on February 6, 1969, Sundstrand was relying on what had been represented to it prior to the termination of the Sundstrand-SKI merger negotiations in January 1969. The district court stated that Ethington gave direct testimony at the trial that Sundstrand relied upon SKI's and Huarisa's representations in the purchase of the Burke stock, and it stated in addition that Sundstrand's reliance was entirely reasonable (M. App. 58). Sundstrand places great weight upon these findings in its Petition to this Court.

However, these findings are clearly erroneous. They were disregarded by the Court of Appeals and should be disregarded by this Court. Ethington did testify as to what Sundstrand relied upon *in entering into the January 9, 1969* agreement (Sun App. 3-6), but neither Ethington nor any other Sundstrand witness (save Sadler) offered any testimony at all as to what Sundstrand relied upon *in purchasing the Burke stock on February 6, 1969,* or why it was purchased two weeks after the Sundstrand-SKI merger negotiations had been abandoned. Sundstrand knows full well that the foregoing findings are erroneous and were made by mistake. Sundstrand proposed these findings in conjunction with findings that Sundstrand had purchased its SKI stock on January 9, 1969. When the district court rejected that theory and found instead that Sundstrand had made its purchase on February 6, 1969, the court neglected to alter a number of related findings which were premised upon a January rather than a February, 1969 purchase, including the findings in question. The district court's mistake was brought about by Sundstrand.

There is no evidence in this case that Sundstrand was induced by defendants to purchase the Burke stock.

6. The Decision Of The Court Of Appeals

The Court of Appeals held that defendants are liable to Sundstrand for $334,785 (plus pre-judgment interest) because defendants wrongfully induced Sundstrand to enter into the January 9, 1969 agreement which obligated Sundstrand to pay $334,785 toward the purchase price of the Burke stock. The Court also held that the January 9, 1969 agreement did not require Sundstrand to pay the $6,360,915 that it paid the Burkes on February 6, 1969. Sundstrand paid that sum, the Court concluded, because it believed it was legally obligated to do so. This was a payment made under a mistake of law; it was not induced by defendants.

The determination that Sundstrand's mistake of law was the cause of its payment of $6,360,915 to the Burke family on February 6, 1969 is amply supported by the record.* Sundstrand believed it had a legal obligation to pay the $6,360,915; it has so maintained throughout this litigation. Sundstrand was wrong, however; it had no such obligation; the money was paid by mistake. Sundstrand suggests that this is a result that defendants did not seek or argue in briefs below. This is not the case; we argued to the Court of Appeals repeatedly (and to the district court, too) that there is only one rational explanation for Sundstrand's $6,360,915 payment, that is, a

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* We need not concern ourselves with the existence or non-existence of a legal opinion (though surely there had to be one). We know that Sundstrand made a mistake.

mistaken belief that the payment was legally required (Sun App. 59-61).*

The determination of the Court of Appeals that Sundstrand purchased the Burke stock because of a mistake of law does not conflict with any valid finding of the district court. As has been seen, the district court's finding that Sundstrand acted in reliance upon defendants' representations in purchasing the Burke stock is in error and was properly disregarded by the Court of Appeals. The evidence showed what Sundstrand relied upon in entering into the January 9, 1969 agreement, and no more.

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* The Court of Appeals' conviction that Sundstrand acted because of a mistake of law was reinforced by the Court's belief that Sundstrand never would have purchased the stock otherwise in view of the adverse information it had about SKI (M. App. 82-83, 84-85, 104, 105).

ARGUMENT

Each of the reasons for granting the requested writ of certiorari was urged in Sundstrand's petition for rehearing *en banc,* and rejected by the Court of Appeals. There is no need for review by this Court. The decision below is not in conflict with decisions of other courts of appeals or with any decisions of this Court. There is no important question for this Court to review. Nor is there any occasion for this Court to exercise its supervisory authority over lower federal courts.

I.

THE COURT OF APPEALS DECISION ON CAUSATION IS EMINENTLY SOUND AND IS NOT IN CONFLICT WITH ANY OTHER DECISIONS WHATEVER.

Sundstrand argues (Pet. pp. 12-17) that the Court of Appeals ignored the principles of causation applicable to actions under Rule 10b-5 because Sundstrand's purchase of the Burke stock on February 6, 1969 was in reality brought about by concurrent causes: (1) Sundstrand's reliance upon defendants' alleged misconduct, as well as (2) Sundstrand's conviction that, no matter what, it was legally obligated to complete the purchase of the Burke stock. And, the argument continues, Sundstrand's supposed reliance upon defendants' misconduct was at least *a* cause of Sundstrand's purchase of the Burke stock, and this is sufficient under the cases to establish causation for the purpose of Rule 10b-5.

There are two answers to this argument. First, Sundstrand could not have (justifiably) relied upon defen-

dants' misconduct in purchasing the Burke stock on February 6, 1969; by that time, Sundstrand had sufficient adverse information about SKI so that it had terminated the merger negotiations and its officers had divested themselves of the bulk of their SKI shares (M. App. 82-83, 84-85, 104, 105). Second, and of greater significance, the Court of Appeals held, and correctly so, that Sundstrand's mistaken conviction that it was legally bound to purchase the Burke stock was *the* cause of the purchase on February 6, 1969 (M. App. 87, 102-104, 105).

This is not a case where there were concurrent causes. On Sundstrand's own theory of this case, maintained from the beginning, Sundstrand's only reason for purchasing the Burke stock was its mistaken belief that it was obligated to make the purchase.

Contrary to Sundstrand's contention, the decision of the Court of Appeals is not in conflict with the decision of this Court in *Affiliated Ute Citizens* v. *United States,* 406 U.S. 128 (1972). *Affiliated Ute* held that, under the circumstances of that case, the withholding of a material fact in connection with the sale of a security warranted an inference of reliance or causation on the part of the seller. In the instant case, any inference of reliance or causation on the part of Sundstrand vanished in the face of the uncontroverted evidence that Sundstrand purchased the Burke stock because it believed it was legally bound to purchase it.

On the peculiar facts involved here, the decision of the Seventh Circuit on the question of causation is correct, and does not conflict with any other decision of either this Court or any court of appeals.

II.

THE DECISION OF THE COURT OF APPEALS DOES NOT CONFLICT WITH DECISIONS OF OTHER COURTS OF APPEALS INTERPRETING THIS COURT'S DECISION IN ERNST & ERNST v. HOCHFELDER, 425 U.S. 183 (1976).

Sundstrand urges (Pet. pp. 17-20) that the decision of the Court of Appeals is in conflict with various decisions of other courts of appeals interpreting *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 183 (1973), primarily the decisions in *Holdsworth* v. *Strong*, 545 F.2d 687 (10th Cir. 1976) and in *Dupuy* v. *Dupuy*, 551 F.2d 1005 (5th Cir. 1977), following *Holdsworth* in principle.

Holdsworth, so far as it is of interest here, holds that if contributory fault of a plaintiff in a Rule 10b-5 case is to cancel reckless or intentional securities fraud on the part of a defendant, the fault of the plaintiff must be gross conduct somewhat comparable to that of defendant (545 F.2d at 693).

The decision below does not conflict with *Holdsworth*. Sundstrand did not fail to recover damages for its purchase of the Burke stock on account of any comparison between its conduct and that of defendants. Sundstrand failed because the evidence demonstrated that Sundstrand purchased the Burke stock on account of a mistake of law, and not because of any conduct of defendants. There was no need to compare Sundstrand's conduct with the conduct of defendants.

Moreover, the Court of Appeals was well aware of *Holdsworth*. It followed *Holdsworth* to the letter in holding that defendants were liable to Sundstrand for inducing it to enter into the stock option transfer agreement on January 9, 1969 (M. App. 81, 100-101).

There is no merit to Sundstrand's assertion that the decision below conflicts with the decision in *Holdsworth*, or with any other decision for that matter.

III.

THE COURT OF APPEALS' REVERSAL OF THE DISTRICT COURT'S DECISION ON DAMAGES IS WELL SUPPORTED BY THE TRIAL RECORD.

Lastly, Sundstrand argues (Pet. pp. 20-24) that the Court of Appeals' *crucial* determination that Sundstrand purchased the Burke stock because it believed it was obligated to do so is a finding that defendants did not seek and no party briefed on appeal, and Sundstrand says, was expressly, indeed blatantly, predicated upon material not in the trial record.

Contrary to Sundstrand's arguments, defendants have vigorously asserted, and briefed on appeal, that the only rational explanation for Sundstrand's purchase of the Burke stock was its mistaken belief that it was legally bound to make the purchase (Sun App. 59-61).

Also, it is clear from the trial record, as well as from additional material in the record on appeal (S. App. 132, 133, 139, 143), that Sundstrand mistakenly believed that it was obligated to purchase the Burke stock, and that this was the reason for the purchase.

As has been seen, it has been Sundstrand's steadfast position throughout this litigation that it was legally required to purchase the Burke stock on February 6, 1969. Its counsel so stated again and again. Sadler testified in open court that Ethington told him that Sundstrand was going to purchase the Burke stock because "our counsel

feels we are obligated to buy the stock." There can be no question but that the trial record alone supports the proposition that Sundstrand bought the stock because of a mistake of law.

So puzzled was the Court of Appeals at Sundstrand's bizarre behavior that, out of an abundance of caution, it looked under every stone. It examined certain deposition testimony that was in the record on appeal but not in the trial record. Deposition testimony of Ethington, of Sundstrand board chairman Olson, and of Schuette, make it abundantly clear that the Court of Appeals' conclusion was correct: Sundstrand bought the Burke stock because it thought it was legally obligated to do so, and for no other reason.*

Sundstrand's argument that it never needed, and therefore made no effort, to rebut or explain the material not in the trial record (Pet. p. 23) must fall on deaf ears. The material not in evidence merely corroborates the position Sundstrand took throughout the case, as well as the testimony of its president, Sadler, at the trial. Sundstrand had ample opportunity to explain or rebut the testimony of Sadler, but neither Ethington nor any other Sundstrand witness did so.

The Court of Appeals' conscientious examination of purely corroborative deposition testimony in the record on appeal is certainly no basis for this Court to exercise its supervisory power over lower federal courts.

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* Sundstrand has not seen fit to reveal the nature of the deposition testimony that is in the record on appeal but not in the trial record. Out of fairness we have included it in our Appendix (Sun App. 61-86).

IV.

THERE IS NO REASON FOR THIS COURT TO REVIEW THE DECISION BELOW.

No amount of strained argument can convert this case into one warranting review by this Court on certiorari.

The decision below turned on its own facts and, insofar as the issues raised by this Petition are concerned, affects no one but the parties to this case.

There is no conflict of decisions. There is no important question for this Court to review. There is no need for this Court to exercise its supervisory powers.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that Sundstrand's Petition for a Writ of Certiorari should be denied.

September 12, 1977.

Respectfully submitted,

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CERTIFICATE OF SERVICE

This Brief of Respondents in Opposition has been served on Petitioner, pursuant to Rule 33(1) of this Court, by depositing three copies thereof in the United States mail box at 69 West Washington Street, Chicago, Illinois, with first class postage prepaid, addressed to W. Donald McSweeney, Esq., 7200 Sears Tower, 233 South Wacker Drive, Chicago, Illinois 60606, on this 12th day of September, 1977.

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